

**NORTH DAKOTA PUBLIC FINANCE
AUTHORITY**
(A Component Unit of the State of North Dakota)

***FINANCIAL STATEMENTS
DECEMBER 31, 2005 AND 2004***

NORTH DAKOTA PUBLIC FINANCE AUTHORITY

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INDEPENDENT AUDITOR'S REPORT

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

We have audited the accompanying basic financial statements of the **North Dakota Public Finance Authority**, a component unit of the State of North Dakota, as of and for the years ended December 31, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of the **North Dakota Public Finance Authority's** management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the **North Dakota Public Finance Authority** as of December 31, 2005 and 2004, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 25, 2006 on our consideration of **North Dakota Public Finance Authority's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the **North Dakota Public Finance Authority**. The accompanying supplemental information on pages 28 through 31 are presented for purpose of additional analysis and are not a required part of the basic financial statements of the **North Dakota Public Finance Authority**. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink that reads "Erik Sully LLP". The signature is written in a cursive, flowing style.

Bismarck, North Dakota
January 25, 2006

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2005 AND 2004
(In Thousands)

The discussion and analysis of the financial performance of the North Dakota Public Finance Authority (PFA) that follows is meant to provide additional insight into the PFA's activities for the years ended December 31, 2005 and 2004. The North Dakota Public Finance Authority changed its name in FY 2005 from the North Dakota Municipal Bond Bank. Please read it in conjunction with the PFA's financial statements and footnotes, which are presented within this report.

FINANCIAL HIGHLIGHTS:

Municipal securities (loans outstanding) increased 5% from \$199,221 in 2004 to \$209,112 in 2005. SRF loans are funded with grant revenues and bond proceeds, which are invested until loans are funded. Grant revenues increased by \$4,853 as grants were utilized to fund loans until bond proceeds were available mid-year. Investments increased by \$31,805 as bond proceeds were invested and will be utilized to fund future loan requests. In 2005, there was \$24,702 of SRF loans funded as compared to \$15,516 in 2004. The PFA anticipates loan demand will continue to remain strong as the ND Health Departments Intended Use Plan continues to grow.

The PFA's rebate due to the Internal Revenue Service increased by \$45. In 2005, rebate payments totaling \$111 were made to the IRS. There were no rebate payments made to the IRS in 2004. As of year-end, the Series 1993A and 1996A SRF bonds' respective final and ten-year rebate payments totaling \$215 of the rebate liability are considered current.

Standard and Poor's upgraded the Capital Financing Program's rating from A- to A in 2005. The PFA did not issue bonds under its Capital Financing Program in 2005. In 2004, \$880 of bonds was issued under this program. The State Revolving Fund Loan Program (rated Aaa by Moody's) issues bonds to provide the required match to receive capitalization grants from the EPA. The PFA issued \$36,210 of SRF bonds in 2005. The proceeds of the SRF series 2005A were used to refund SRF Series 1993A bonds, partially refund SRF Series 1998A bonds and provide state match and leveraged funds for the program. In 2004, the PFA issued \$11,790 of SRF Series 2004A bonds, which were used to partially refund SRF Series 2000A. The PFA does not anticipate issuing State Revolving Fund Program bonds in 2006.

The growing State Revolving Fund Program helped the PFA's total assets increase \$41,395 to \$380,800. The balance sheet indicates that the PFA continues to have adequate resources to provide for bond repayments. Change in net assets of the PFA resulted in an increase of \$22,262 providing the PFA with an overall strong financial position. Grant proceeds account for a significant portion of net assets. Federal law provides that grants may only be expended for SRF program purposes. Net assets are also restricted for debt service of bond issues or for the purchase of municipal securities. As of December 31, 2005, the PFA had \$24,160 of commitments to extend credit.

REQUIRED FINANCIAL STATEMENTS:

The discussion and analysis are intended to serve as an introduction to the PFA's financial statements. The financial statements of the PFA provide accounting information similar to that of many other business entities. The Balance Sheets summarize the assets and liabilities, with the difference between the two reported as net assets. It also serves as the basis for analysis of the soundness and liquidity of the PFA. The Statements of Revenues, Expenses and Changes in Fund Net Assets summarize the PFA's operating performance for the two years. The Statements of Cash Flows summarizes the flow of cash through the PFA as it conducts its business.

CONDENSED BALANCE SHEETS
DECEMBER 31,

	2005	2004	Dollar Variance	Percentage Variance
ASSETS				
CURRENT ASSETS - UNRESTRICTED	\$ 2,161	\$ 2,566	\$ (405)	-15.78%
CURRENT ASSETS - RESTRICTED	24,097	20,169	3,928	19.48%
NONCURRENT ASSETS - RESTRICTED	354,542	316,670	37,872	11.96%
TOTAL ASSETS	<u>\$ 380,800</u>	<u>\$339,405</u>	<u>\$ 41,395</u>	<u>12.20%</u>
LIABILITIES				
CURRENT LIABILITIES	\$ 12,092	\$ 10,927	\$ 1,165	10.66%
NONCURRENT LIABILITIES	166,370	148,402	17,968	12.11%
TOTAL LIABILITIES	<u>178,462</u>	<u>159,329</u>	<u>19,133</u>	<u>12.01%</u>
NET ASSETS				
UNRESTRICTED	2,148	2,556	(408)	-15.96%
RESTRICTED FOR DEBT SERVICE	71,272	89,737	(18,465)	-20.58%
RESTRICTED FOR LOAN PURPOSES	128,918	87,783	41,135	46.86%
TOTAL NET ASSETS	<u>202,338</u>	<u>180,076</u>	<u>22,262</u>	<u>12.36%</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 380,800</u>	<u>\$339,405</u>	<u>\$ 41,395</u>	<u>12.20%</u>

Cash and Investments

Certain PFA cash and investments, which are included in the restricted current and noncurrent assets, are restricted for the debt service of bond issues or for the purchase of municipal securities. Additional discussion of these investments can be found at Note 3 to the financial statements.

Municipal Securities

Obligations of North Dakota political subdivisions are classified separately on the balance sheet as "municipal securities" and included in the restricted current and noncurrent assets of the condensed Balance Sheet. These investment securities are primarily city, school district and water district obligations and are pledged to the various bond issues. No losses for market value declines are anticipated and an allowance has not been provided. Note 3 to the financial statements contain further information regarding municipal securities.

MANAGEMENT'S DISCUSSION AND ANALYSIS – page 3
(In Thousands)

Bonds Payable

In order to provide local political subdivisions with funds to finance projects, the PFA has issued bonds to facilitate the purchase of the political subdivision's municipal securities. The bonds payable are included in the restricted current and noncurrent liabilities of the preceding statement. The bonds are direct obligations of the PFA and are secured by municipal securities purchased under the applicable resolutions, interest earnings and certain accounts established pursuant to the applicable bond resolutions. Further details are contained in Note 4 to the financial statements.

Rebate Due to IRS

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as a rebate, once every five years, to the U.S. Treasury. This liability is included in the current and noncurrent liabilities. Note 8 to the financial statements contain additional information.

CONDENSED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
YEARS ENDED DECEMBER 31,

	<u>2005</u>	<u>2004</u>	<u>Dollar Variance</u>	<u>Percentage Variance</u>
OPERATING REVENUES				
Investment income	\$ 6,132	\$ 6,120	\$ 12	0.20%
Administrative fees and other	929	916	13	1.42%
	<u>7,061</u>	<u>7,036</u>	<u>25</u>	<u>0.36%</u>
NONOPERATING REVENUE				
Grant and set-asides	16,267	11,414	4,853	42.52%
Investment income	8,384	7,481	903	12.07%
	<u>24,651</u>	<u>18,895</u>	<u>5,756</u>	<u>30.46%</u>
TOTAL REVENUE	<u>31,712</u>	<u>25,931</u>	<u>5,781</u>	<u>22.29%</u>
OPERATING EXPENSES				
Interest expense	7,854	7,926	(72)	-0.91%
State Revolving Fund expenses	1,065	883	182	20.61%
Rebate due to IRS	156	137	19	13.87%
Amortization of bond issue costs	212	153	59	38.56%
Other	163	152	11	7.24%
	<u>9,450</u>	<u>9,251</u>	<u>199</u>	<u>2.15%</u>
CHANGE IN NET ASSETS	<u>22,262</u>	<u>16,680</u>	<u>5,582</u>	<u>33.47%</u>
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>180,076</u>	<u>163,396</u>	<u>16,680</u>	<u>10.21%</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 202,338</u>	<u>\$ 180,076</u>	<u>\$ 22,262</u>	<u>12.36%</u>

Note 1 to the financial statements contains discussion of several of the various operating revenue and expense items pertaining to PFA operations.

Grant and set-asides

Under an agreement with the North Dakota Department of Health, the PFA assists in administering the State Revolving Loan Fund. The grant proceeds are classified as nonoperating revenue in the Statement of Revenues, Expenditures and Changes in Net Assets.

The purpose of the Loan Fund is to provide low cost financing to local political subdivisions to finance wastewater disposal system projects and drinking water projects. The federal Environmental Protection Agency (EPA) provides funds to finance approximately 80 percent of the cost of the projects. The state finances its 20 percent share of the cost through bonds issued by the PFA.

Economic Factors and Budgetary Information

Note 1 to the financial statements discusses the PFA's economic dependence on North Dakota political subdivision municipal securities obligations.

As discussed in financial statement Note 1, the PFA, an agency of the Industrial Commission, operates through a biennial appropriation provided by the State Legislature. The PFA prepares a biennial budget as a part of the Industrial Commission's budget, which is included in the Governor's budget that is presented to the General Assembly at the beginning of each legislative session. The PFA has a continuous appropriation of income from operations. Changes to the appropriation not falling under the continuing appropriation are subject to approval by the State Emergency Commission.

Contacting the North Dakota Public Finance Authority's financial management:

The information in this report is intended to provide the reader with an overview of the PFA's operations along with the PFA's accountability for those operations. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the North Dakota Public Finance Authority, PO Box 5509, Bismarck, ND 58506-5509.

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
BALANCE SHEETS
DECEMBER 31, 2005 AND 2004
(In Thousands)

	<u>2005</u>	<u>2004</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents - unrestricted	\$ 2,161	\$ 2,566
Restricted		
Restricted cash and cash equivalents	1,572	1,602
Interest receivable	3,850	3,404
Investments	8,560	5,634
Municipal securities	10,084	9,529
Advance to Bank of North Dakota	31	-
Total restricted current assets	<u>24,097</u>	<u>20,169</u>
Total current assets	<u>26,258</u>	<u>22,735</u>
NONCURRENT ASSETS - RESTRICTED		
Investments	148,558	119,679
Municipal securities	199,028	189,692
Deferred bond financing costs, net	1,262	1,246
Advance to Bank of North Dakota	5,694	6,053
Total restricted noncurrent assets	<u>354,542</u>	<u>316,670</u>
Total assets	<u>\$ 380,800</u>	<u>\$ 339,405</u>
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	\$ 16	\$ 33
Rebate due to IRS	215	110
Bonds payable	9,620	9,150
Interest payable	2,210	1,634
Advance from Bank of North Dakota	31	-
Total current liabilities	<u>12,092</u>	<u>10,927</u>
NONCURRENT LIABILITIES		
Rebate due to IRS	278	338
Bonds payable, net	160,459	142,011
Advance from Bank of North Dakota	5,633	6,053
Total noncurrent liabilities	<u>166,370</u>	<u>148,402</u>
Total liabilities	<u>178,462</u>	<u>159,329</u>
NET ASSETS		
Unrestricted	2,148	2,556
Restricted for debt service	71,272	89,737
Restricted for loan purposes	128,918	87,783
Total net assets	<u>202,338</u>	<u>180,076</u>
Total liabilities and net assets	<u>\$ 380,800</u>	<u>\$ 339,405</u>

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
YEARS ENDED DECEMBER 31, 2005 AND 2004
(In Thousands)

	<u>2005</u>	<u>2004</u>
OPERATING REVENUES		
Investment income	\$ 6,132	\$ 6,120
Administrative fees and other	929	916
	<u>7,061</u>	<u>7,036</u>
OPERATING EXPENSES		
Interest expense	7,854	7,926
State Revolving Fund administration	465	488
State Revolving Fund set-asides	600	395
Rebate due to IRS	156	137
Salaries and benefits	111	112
Amortization of bond issue costs	212	153
Operating	44	31
Paying agent fees	8	9
	<u>9,450</u>	<u>9,251</u>
OPERATING LOSS	<u>(2,389)</u>	<u>(2,215)</u>
NONOPERATING REVENUE		
Grant and set-asides	16,267	11,414
Investment income	8,384	7,481
	<u>24,651</u>	<u>18,895</u>
CHANGE IN NET ASSETS	22,262	16,680
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>180,076</u>	<u>163,396</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 202,338</u>	<u>\$ 180,076</u>

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004
(In Thousands)

	<u>2005</u>	<u>2004</u>
OPERATING ACTIVITIES		
Receipts of administrative fees from customers	\$ 929	\$ 917
Payments to service providers	(1,134)	(952)
Payments to employees	(112)	(112)
Payment of rebate to IRS	(111)	-
NET CASH USED FOR OPERATING ACTIVITIES	<u>(428)</u>	<u>(147)</u>
NONCAPITAL FINANCING ACTIVITIES		
Grant and set-asides	16,267	11,414
Interest paid on bonds payable	(7,101)	(7,544)
Bond financing costs	(286)	(124)
Principal payment on advance from Bank of North Dakota	(388)	(407)
Proceeds from bond premiums	1,216	509
Proceeds from issuance of bonds payable	36,210	12,670
Principal payments on bonds payable	(18,626)	(21,106)
NET CASH FROM (USED FOR) NONCAPITAL FINANCING ACTIVITIES	<u>27,292</u>	<u>(4,588)</u>
INVESTING ACTIVITIES		
Interest received on investments and municipal securities	14,069	13,551
Collection of advance to Bank of North Dakota	328	407
Proceeds from maturities and sales of investments	49,223	38,809
Purchases of investments	(80,438)	(44,088)
Proceeds from maturities of municipal securities	14,228	12,416
Purchases of municipal securities	(24,709)	(16,404)
NET CASH FROM (USED FOR) INVESTING ACTIVITIES	<u>(27,299)</u>	<u>4,691</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(435)	(44)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>4,168</u>	<u>4,212</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 3,733</u>	<u>\$ 4,168</u>
CASH AND CASH EQUIVALENTS - UNRESTRICTED	\$ 2,161	\$ 2,566
RESTRICTED CASH AND CASH EQUIVALENTS	<u>1,572</u>	<u>1,602</u>
TOTAL CASH AND CASH EQUIVALENTS	<u>\$ 3,733</u>	<u>\$ 4,168</u>

(continued on next page)

STATEMENTS OF CASH FLOWS – page 2
(In Thousands)

	<u>2005</u>	<u>2004</u>
RECONCILIATION OF OPERATING LOSS TO TO NET CASH USED FOR OPERATING ACTIVITIES		
Operating loss	\$ (2,389)	\$ (2,215)
Adjustments to reconcile operating loss to net cash used for operating activities		
Amortization of bond financing costs	211	153
Net accretion of discount on bonds payable	947	(750)
Reclassification of investment income and expense to other activities	774	2,554
Changes in assets and liabilities		
Accounts payable	(16)	(28)
Rebate due IRS	45	139
NET CASH USED FOR OPERATING ACTIVITIES	<u>\$ (428)</u>	<u>\$ (147)</u>

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
STATEMENT OF APPROPRIATIONS
EIGHTEEN MONTHS ENDED JUNE 30, 2005 AND SIX MONTHS ENDED DECEMBER 31, 2005
(In Thousands)

Note: Only appropriations of specific amounts are included in this statement. A reconciliation to the operating expenses on the December 31, 2005 and 2004 statement of revenues and expenses follows:

	2003-2005 Appropriations	7-1-03- 12-31-03 Expenditures	1-1-04- 12-31-04 Expenditures	1-1-05- 6-30-05 Expenditures	Unexpended Appropriations at 12-31-04	2005-2007 Appropriations	7-1-05- 12-31-05 Expenditures	Unexpended Appropriations at 12-31-05
Salaries and wages	\$ 311	\$ 57	\$ 112	\$ 54	\$ 88	\$ 334	\$ 57	\$ 277
Operating expenses	243	10	31	30	172	223	14	209
Total administrative expenses	554	67	143	84	260	557	71	486
Equipment	12	-	-	-	12	-	-	-
Total expenses	\$ 566	\$ 67	\$ 143	\$ 84	\$ 272	\$ 557	\$ 71	\$ 486
Total appropriation expenditures for year ended December 31		\$ 155	\$ 143					
Interest expense		7,853		7,925				
Depreciation and amortization		211		153				
State Revolving Fund administrative fees		1,066		882				
Rebate due to IRS		157		138				
Administrative and operating expenses paid out of general operating funds - paying agent fees		8		10				
Total operating expenses		\$ 9,450	\$ 9,251					

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 AND 2004
(In Thousands)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

The North Dakota Public Finance Authority (PFA) was established July 1, 1975, by the North Dakota Legislature, as provided in Chapter 6-09.4 of the North Dakota Century Code, as a separate agency of the State of North Dakota. The purpose of the PFA is to make funds available for borrowing by North Dakota political subdivisions through the issuance of its bonds and the purchase of municipal securities of the political subdivisions. The PFA has been granted all powers required in order to accomplish this purpose and is under the control and management of the North Dakota Industrial Commission.

Reporting Entity

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, the PFA should include all component units over which the PFA exercises such aspects as (1) appointing a voting majority of an organization's governing body and (2) has the ability to impose its will on that organization, or (3) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the PFA. GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, an Amendment of GASB Statement 14, further defined reporting units as a legally separate, tax exempt affiliated organization that meet all of the following criteria:

- The economic resources of the organization entirely or almost entirely directly benefit the PFA or its constituents, and
- The PFA or its component units are entitled to or can otherwise access, a majority of the economic resources of the organization, and
- The economic resources that the PFA is entitled to, or can otherwise access, are significant to the PFA.

Based on the criteria of GASB Statement No. 14 and 39, no organizations were determined to be part of the reporting entity. The PFA is included as a discretely presented component unit within the State of North Dakota's reporting entity.

Budgetary Process

The PFA operates through a biennial appropriation provided by the State Legislature. The PFA prepares a biennial budget which is included in the Governor's budget that is presented to the General Assembly at the beginning of each legislative session. The General Assembly enacts the budgets of the various state departments through passage of specific appropriation bills. The Governor has line item veto powers over all legislation subject to legislative override. Once passed and signed, the appropriation becomes the PFA's financial plan for the next two years. The PFA has a continuous appropriation of income from operations. Changes to the appropriation not falling under the continuing appropriation are subject to approval by the State Emergency Commission.

The Statement of Appropriations has been prepared using the accrual basis of accounting and includes only those expenses for which an appropriation has been established.

NOTES TO FINANCIAL STATEMENTS

Basis of Accounting and Measurement Focus

The North Dakota Public Finance Authority is presented in the accompanying financial statements as a proprietary fund type - an enterprise fund.

An enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent is that costs of providing goods or services to the general public or other funds on a continuing basis be financed or recovered primarily through user charges. The PFA recovers its costs through administrative charges to municipalities and earnings on administrative funds. The Program revenues include 1) Income from receivables and 2) Administrative fees. The Non Program revenues include 1) Investment income and 2) Income from grants and set-asides.

As a proprietary fund type, the PFA accounts for its transactions using the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

The accompanying financial statements of the North Dakota Public Finance Authority follow the pronouncements of the Governmental Accounting Standards Board (GASB), which is the nationally accepted standard-setting body for establishing generally accepted accounting principles for governmental entities. In accordance with Governmental Accounting Standards Board Statement No. 20, the PFA follows all applicable GASB Pronouncements as well as following Financial Accounting Standards Board pronouncements issued on or before November 30, 1989 unless those pronouncements conflict with GASB pronouncements.

Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect reported amounts of assets and liabilities at the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Concentration of Credit Risk

Municipal securities primarily consist of obligations of cities, school districts and water organizations. The PFA performs credit evaluations and, in some instances, municipal securities are collateralized by property and leases. Generally, the PFA maintains a security interest until related receivables are collected. Municipal securities are due under terms corresponding with applicable bonds. All customers are located in the state of North Dakota.

NOTES TO FINANCIAL STATEMENTS

Cash and Cash Equivalents

The PFA considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. The PFA follows the bond indenture documentation on satisfying requirements for unrestricted and restricted cash and cash equivalents.

Investments

Investments are reported at fair value. All investment income, including changes in the fair value of investments, is recognized in the statement of revenues, expenses, and changes in fund net assets. A portion of the PFA's investments consists of nonparticipating contracts. These instruments are reported at cost. The PFA follows the bond indenture documentation on satisfying requirements for unrestricted and restricted investments.

Funds held by trustees or the PFA under bond resolutions are to be invested to the fullest extent possible in investment obligations selected by the PFA. The maturity date or the date on which such investment obligations may be redeemed shall coincide as nearly as practicable with the date or dates on which moneys in the funds or accounts for which the investments were made will be required. The restricted bond accounts have their moneys invested in various debt securities such as U.S. Treasury securities, U.S. Government Agency securities, tax-exempt obligations of states and political subdivisions, certificates of deposit, and investment contracts.

Deferred Bond Financing Costs

Bond issuance costs are being amortized over the life of the bonds using the interest method.

Equipment and Furnishings

Equipment and furnishings are stated at cost, net of accumulated depreciation. Equipment and furnishings with a cost of \$5,000 or more per unit are capitalized and reported in the accompanying financial statements. Depreciation is computed using the straight-line method over the estimated useful lives of the assets which range from five to ten years.

Accumulated Unpaid Vacation and Sick Pay

Annual leave and sick leave are a part of permanent employees' compensation as set forth in Section 54-06-14 of the North Dakota Century Code. Annual leave is earned based on tenure of employment, within a range of a minimum of one working day per month of employment, to a maximum of two working days per month of employment, to be fixed by rules and regulations adopted by the employing unit. In general, accrued annual leave cannot exceed 30 days at each year-end, as set by the Agency. Employees are paid for unused annual leave upon termination or retirement.

Sick leave is earned based on tenure at the rate of one working day per month of employment. There are no limitations on the amount of sick leave that an employee can accumulate. Employees who have ten continuous years of service are paid one-tenth of their accumulated sick leave upon leaving service under chapter 54-52 of the North Dakota Century Code.

Vacation and sick leave are immaterial as of December 31, 2005 and 2004, and are not accrued.

NOTES TO FINANCIAL STATEMENTS

Restricted Net Assets

The PFA administers the SRF federal grant programs for the North Dakota Department of Health. Grant proceeds account for a significant portion of net assets. Federal law provides that the grants may only be expended for SRF program purposes. Net assets are also restricted for debt service of bond issues or for the purchase of municipal securities. The PFA follows the CFP and SRF bond indenture for the repayment of restricted net assets.

Operating and Non-operating Revenues

Operating revenues consist of sales of goods and services, quasi-external operating transactions with other funds, grant revenue for specific activities that are considered to be operating activities of the grantor, receipts from other agencies for reimbursement of operating transactions and other miscellaneous revenue. Grants that would qualify as an operating activity are those that do not subsidize an existing program, rather they finance a program the agency would not otherwise undertake.

All other revenues that do not meet the above criteria are classified as non-operating.

Administrative Fee Revenue

All loans originated by the PFA are charged an administration fee. These fees are used to cover the costs incurred in the administration of the loan programs. Income is recorded when the fees are received.

Grant and Set-Asides Revenue

The SRF Program grants, received from the United States Environmental Protection Agency, are to be used to make below-market interest rate loans to political subdivisions for the purpose of financing authorized projects. In addition, the Drinking Water SRF Program is allowed to “set-aside” a percentage of each grant award, which is expended for administration, technical assistance and source water assessment programs.

State Revolving Fund Administration Expense

State Revolving Fund administration expenses are incurred by the PFA and North Dakota Department of Health in administration of the State Revolving Loan Programs.

State Revolving Fund Set-Asides Expenses

The Drinking Water SRF Program is allowed to “set-aside” a percentage of each grant award, which is expended for administration, technical assistance and source water assessment programs.

Rebate Due to IRS

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as rebate, once every five years, to the U.S. Treasury. Annually, rebate is calculated and the liability is accordingly adjusted.

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - DEPOSITS AND INVESTMENTS

DEPOSITS

The North Dakota Public Finance Authority is required to maintain its deposits at the Bank of North Dakota. As of December 31, 2005, the PFA had the following deposits (amounts in the thousands):

	<u>Bank Balance</u>
Cash and cash equivalents	\$ 3,733
Certificates of deposit	8,475
Certificates of deposit recorded as advances to Bank of North Dakota	5,725
Bank investment contracts - Bank of North Dakota	13,373
Canadian Imperial Bank of Commerce	<u>9,573</u>
Total deposits	<u>\$ 40,879</u>

Custodial and Concentration Credit Risk

For a deposit, the custodial credit risk that, in the event of the failure of a depository financial institution, the PFA will not be able to recover collateral securities that are in the possession of an outside party. The PFA's deposits are uncollateralized. All of the deposits, except Canadian Imperial Bank of Commerce, are with the Bank of North Dakota.

INVESTMENTS

NDCC 6-09.4-7 authorizes the PFA to invest any funds in the same manner as permitted for investment of funds belonging to the state or the Bank of North Dakota. The PFA does have a formal investment policy. Also, the General Bond Resolution and Master Trust Indenture specify the permitted investments. The PFA follows those stipulations when investing funds.

Funds held by trustees or the PFA under bond resolutions are to be invested to the fullest extent possible in investment obligations selected by the PFA. The maturity date or the date on which such investment obligations may be redeemed shall coincide as nearly as practicable with the date or dates on which moneys in the funds or accounts for which the investments were made will be required. The restricted bond accounts may have their moneys invested in various debt securities such as U.S. Treasury securities, U.S. Government Agency securities, guaranteed investment contracts and certificates of deposit. There is no limit on the amount the PFA may invest in any one issuer.

NOTES TO FINANCIAL STATEMENTS

As of December 31, 2005, the PFA had the following investments (amounts are in thousands):

	<u>Fair Value</u>
MBIA	\$ 40,832
IXIS Funding Corp.	18,960
GE Funding	21,212
Trinity Plus Funding Company	43,644
US Treasuries	<u>70</u>
Total guaranteed investment contracts	<u>\$ 124,718</u>

Credit Risk

The PFA's North Dakota State Revolving Fund Program Master Trust Indenture restricts investments in Guaranteed Investment Contracts (GICs) and Bank Investment Contracts (BICs) issued, at the time the contract is entered into, a long-term debt rating by Moody's, at least equal to the better of (i) "A" or (ii) the then current rating assigned by Moody's to the Bonds without regard to credit enhancement for long-term obligations.

Concentration of Credit Risk

Each of the above listed investments represents 5 percent or more of total investments.

NOTE 3 - MUNICIPAL SECURITIES

Obligations of North Dakota political subdivisions are classified separately on the balance sheet as "municipal securities." These investment securities are primarily obligations of cities, school districts and water organizations, and are pledged to the various bond issues. Due to the maturity of these securities, a market value is not readily available. The PFA intends to hold these securities to maturity. No losses for market value decline are anticipated and an allowance has not been provided. The PFA had the following municipal securities as of December 31:

	<u>2005</u>	<u>2004</u>
Capital financing program	\$ 25,453	\$ 29,976
State revolving fund program	<u>183,659</u>	<u>169,245</u>
	209,112	199,221
Less current portion	<u>10,084</u>	<u>9,529</u>
	<u>\$ 199,028</u>	<u>\$ 189,692</u>

NOTES TO FINANCIAL STATEMENTS

NOTE 4 - BONDS PAYABLE

Changes in Bonds Payable

The following is a summary of changes in bonds payable for the years ended December 31, 2005 and 2004:

Balance, December 31, 2003	\$ 158,901
Issuance of bonds payable	12,670
Principal payments on bonds payable	(19,660)
Net accretion of premiums and discounts on bonds payable	<u>(751)</u>
Balance, December 31, 2004	151,160
Issuance of bonds payable	36,210
Principal payments on bonds payable	(18,240)
Net accretion of premiums and discounts on bonds payable	<u>949</u>
Balance, December 31, 2005	<u><u>\$ 170,079</u></u>

Bonds Payable

The bonds of the PFA have been issued to provide financing to purchase municipal securities in order to provide local political subdivisions with funds to finance local projects. The bonds are direct obligations of the PFA and are secured by municipal securities purchased under the applicable resolutions, interest earnings and certain accounts established pursuant to the applicable bond resolutions.

Maturities of Bonds Payable

Maturities of principal and interest on all bonds are as follows:

<u>Years Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Debt Service</u>
2006	\$ 9,620	\$ 8,070	\$ 17,690
2007	10,880	7,309	18,189
2008	11,075	6,821	17,896
2009	11,465	6,340	17,805
2010	10,830	5,851	16,681
2011-2015	55,155	21,995	77,150
2016-2020	41,790	9,931	51,721
2021-2025	18,635	2,230	20,865
2026-2028	474	40	514
Premiums, net of discounts	155	(155)	-
	<u><u>\$ 170,079</u></u>	<u><u>\$ 68,432</u></u>	<u><u>\$ 238,511</u></u>

NOTES TO FINANCIAL STATEMENTS

The following summarizes the PFA's bonds outstanding at December 31, 2005 and 2004:

Description and Due Date	Interest Rate	Original Value	2005	2004
Series 1990-CFP Serial Bonds 12/1/03-12/1/05	7.30-7.40	\$ 3,750	\$ -	\$ 25
Series 1991-CFP Serial Bonds 12/1/03-12/1/06	6.25	6,225	10	20
Series 1992-CFP Serial Bonds 6/1/03-6/1/07	6.50	13,535	10	15
Series 1993-CFP Serial Bonds 6/1/03-6/1/13	4.50-5.75	7,905	2,340	2,795
Series 1993-SRF Serial Bonds 10/1/03-10/1/14 (net of discount)	5.55-6.25	20,220	-	4,172
Series 1994-CFP Serial Bonds - 6/1/03-6/1/04	5.70	6,305	-	-
Series 1995-CFP Serial Bonds 6/1/03-6/1/15	5.20-6.00	2,505	70	1,205
Series 1995-SRF Serial Bonds 10/1/03-10/1/07 (net of discount)	5.90-6.40	6,975	672	978
Series 1996-CFP Serial Bonds 6/1/03-6/1/16	5.20-6.60	3,365	545	665
Series 1996-SRF Serial Bonds 10/1/03-10/1/17 (net of premium)	5.10-6.00	29,845	1,825	3,066
Series 1997-CFP Serial Bonds 6/1/03-6/1/17	4.60-7.15	15,345	6,840	7,380
Series 1998-CFP Serial Bonds 6/1/03-6/1/23 (net of deferred loss on refunding of \$134)	4.10-5.25	9,695	4,863	5,501
Series 1998-SRF Serial Bonds 10/1/03-10/1/19 (net of premium)	4.00-5.50	35,965	23,863	29,340

(continued on next page)

NOTES TO FINANCIAL STATEMENTS

Description and Due Date	Interest Rate	Original Value	2005	2004
Series 1999 Serial Bonds 4/1/03-4/1/14 (net of deferred loss on refunding of \$30)	10.00	10,285	5,443	6,343
Series 1999-CFP Serial Bonds 6/1/03-6/1/23	4.80-8.25	4,530	1,875	1,955
Series 2000-SRF Serial Bonds 10/1/03-10/1/21 (net of discount)	5.00-5.35	16,725	3,194	3,740
Series 2001-CFP Serial Bonds 6/1/03-6/1/21	4.70 - 6.00	735	635	660
Series 2001-SRF Serial Bonds 10/1/03-10/1/21 (net of discount) (net of deferred loss on refunding of \$809)	3.20 - 5.00	23,725	20,746	21,873
Series 2002-CFP Serial Bonds 6/1/03-6/1/28	3.00 - 5.60	1,700	1,485	1,545
Series 2003-CFP Serial Bonds 6/1/04-6/1/28	2.95 - 5.40	1,495	1,430	1,470
Series 2003-SRF Serial Bonds 10/1/03-10/1/23 (net of premium) (net of deferred loss on refunding of \$1,977)	2.00 - 5.00	47,250	45,526	46,687
Series 2004-CFP Serial Bonds 6/1/05-6/1/24	2.00 - 4.90	880	830	880
Series 2004-SRF Serial Bonds 10/1/05-10/1/21 (net of premium) (net of deferred loss on refunding of \$1,425)	2.00 - 4.75	11,790	10,873	10,846
Series 2005-SRF Serial Bonds 10/1/06-10/1/23 (net of premium) (net of deferred loss on refunding of \$386)	3.00 - 5.00	36,210	37,004	
			<u>\$ 170,079</u>	<u>\$ 151,161</u>

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NOTES TO FINANCIAL STATEMENTS

On July 27, 2005 the PFA issued \$36,210 of revenue bonds (Series 2005A SRF Bonds) with an average interest rate of 3.82 percent. The net proceeds of the refunding portion of the bonds were deposited in an irrevocable trust with an escrow agent to provide for all the future debt service payments on the refunded bonds. As of December 31, 2005, \$4,070 of bonds outstanding is considered defeased and the liability has been removed from the balance sheet. The reacquisition price exceeded the net carrying amount of the old debt by \$386. This amount is being netted against the new debt and amortized over the life of the refunded debt, which is the same as the life of the new debt issued. This advance refunding was undertaken to reduce total debt service payments over the next 9 years by \$806 and resulted in an economic gain of \$660.

The PFA issued \$11,790 of revenue bonds (Series 2004A SRF Bonds) with an average interest rate of 4.16 percent on October 5, 2004. The net proceeds were deposited in an irrevocable trust with an escrow agent to provide for all the future debt service payments on the refunded bonds. As of December 31, 2005, \$11,005 of bonds outstanding is considered defeased and the liability has been removed from the balance sheet. The reacquisition price exceeded the net carrying amount of the old debt by \$1,446. This amount is being netted against the new debt and amortized over the life of the refunded debt, which is the same as the life of the new debt issued. This advance refunding was undertaken to reduce total debt service payments over the next 17 years by \$919 and resulted in an economic gain of \$679.

NOTE 5 - ADVANCE FROM BANK OF NORTH DAKOTA

Changes in Advance from Bank of North Dakota

The following is a summary of changes in advance from the Bank of North Dakota for the year ended December 31, 2005 and 2004:

Balance, December 31, 2003	\$ 6,460
Principal payments on advance from Bank of North Dakota	(407)
Balance, December 31, 2004	<u>6,053</u>
Principal payments on advance from Bank of North Dakota	<u>(328)</u>
Balance, December 31, 2005	<u><u>\$ 5,725</u></u>

NOTES TO FINANCIAL STATEMENTS

Maturities of Advance from Bank of North Dakota

Maturities of principal and interest on the advance are as follows:

Years Ending December 31,	Principal	Interest	Total Debt Service
2006	\$ 31	\$ 269	\$ 300
2007	143	264	407
2008	344	247	591
2009	232	229	461
2010	-	223	223
2011-2015	3,281	907	4,188
2016-2019	1,694	296	1,990
	<u>\$ 5,725</u>	<u>\$ 2,435</u>	<u>\$ 8,160</u>

NOTE 6 - PENSION PLAN

The North Dakota Public Finance Authority participates in the North Dakota Public Employees' Retirement System (NDPERS) administered by the State of North Dakota. The following is a brief description of the plan.

NDPERS is a cost-sharing multiple-employer defined benefit pension plan covering substantially all classified employees of the North Dakota Public Finance Authority. The plan provides retirement, disability, and death benefits. If an active employee dies with less than three years of credit service, a death benefit equal to the value of the employee's accumulated contributions, plus interest, is paid to the employee's beneficiary. If the employee has earned more than three years of credited service, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the employee's accrued normal retirement benefit, or 60 monthly payments equal to the employee's accrued normal retirement benefit calculated as if the employee were age 65 the day before death occurred or monthly payments in an amount equal to the employee's accrued 100% joint and survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the employee's accumulated pension benefits are paid, the balance will be paid to the surviving spouse's designated beneficiary.

Eligible employees, who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits that are equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the employee must meet the criteria established by the Retirement Board for being considered totally disabled.

Employees are entitled to unreduced monthly pension benefits equal to 2% of their final average salary for each year of service beginning when the sum of age and years of credited service equal or exceed 85, or at normal retirement age (65). The plan permits early retirement at ages 55-64, with three or more years of service.

NOTES TO FINANCIAL STATEMENTS

Benefit and contribution provisions are administered in accordance with chapter 54-52 of the North Dakota Century Code. This state statute requires that 4% of the participant's salary be contributed to the plan by either the employee or by the employer under a "salary reduction" agreement. The North Dakota Public Finance Authority has implemented a salary reduction agreement and is currently contributing the employee's share. In addition to the 4.12% employer contribution, the employer is required to contribute 1% of each participating employee's gross wage to a prefunded retiree health insurance program. The North Dakota Public Finance Authority is required to contribute 4.12% of each participant's salary as the employer's share. The required contributions are determined using an entry age normal actuarial funding method. The North Dakota Retirement Board was created by the State Legislature and is the governing authority of NDPERS. The North Dakota Public Finance Authority's required and actual contributions to NDPERS were \$3, \$3 and \$3 for the years ended December 31, 2005, 2004, and 2003.

NDPERS issues a publicly available financial report that includes financial statements and the required supplementary information for NDPERS. That report may be obtained by writing to NDPERS; 400 East Broadway, Suite 505; P.O. Box 1657; Bismarck, ND 58502-1657.

NOTE 7 - STATE REVOLVING LOAN FUND

Under an agreement with the North Dakota Department of Health, the PFA assists in administering the State Revolving Loan Fund. The purpose of the Loan Fund is to provide low cost financing to local political subdivisions to finance wastewater disposal system projects and drinking water projects.

The federal Environmental Protection Agency (EPA) provides funds to finance approximately 80 percent of the cost of the projects. The state finances its 20 percent share of the cost through bonds issued by the PFA.

As of December 31, 2005 and 2004, the following Loan Fund transactions had occurred:

	<u>2005</u>	<u>2004</u>
Municipal securities purchased	\$ 24,702	\$ 31,003
EPA grant funds received	16,267	11,414

NOTES TO FINANCIAL STATEMENTS

NOTE 8 - REBATE DUE TO IRS

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as a rebate, once every five years, to the U.S. Treasury. A detail of the cumulative rebate at December 31, 2005 and 2004 is as follows:

	<u>2005</u>	<u>2004</u>
1993A SRF bonds	\$ 10	\$ 8
1995A SRF bonds	7	29
1996A SRF bonds	205	152
1998A SRF bonds	128	86
2000A SRF bonds	19	81
2003A SRF bonds	<u>124</u>	<u>92</u>
Rebate due to IRS	493	448
Current rebate due to IRS	<u>(215)</u>	<u>(110)</u>
Long-term rebate due to IRS	<u>\$ 278</u>	<u>\$ 338</u>

NOTE 9 - RELATED PARTY TRANSACTIONS

All cash accounts of the PFA are deposited in the Bank of North Dakota. All investments are under the safekeeping of the Bank of North Dakota. The Bank of North Dakota acts as paying agent for all bonds and as trustee for the 1999 Bonds and the 1995, 1996, 1998, 2000, 2001, 2003, 2004 and 2005 State Revolving Fund Bonds.

NOTES TO FINANCIAL STATEMENTS

The PFA had the following transactions with related parties summarized as follows:

	<u>2005</u>	<u>2004</u>
Bank of North Dakota		
Cash and cash equivalents - unrestricted	\$ 2,161	\$ 2,566
Cash and cash equivalents - restricted	1,572	1,602
Interest receivable	110	54
Certificates of deposit recorded as investments (current portion of \$7,931)	8,475	6,220
Advance to/from Bank of North Dakota (1)	5,694	6,053
Interest payable	22	16
Bank investment contract (2)	13,373	11,478
Expenses		
Registrar, paying agent and trustee fees	80	80
Account analysis	4	4
Information services	-	-
Letter of credit fees	9	9
Office of the Attorney General		
Legal fees	12	12
Information Technology Department		
Telecommunications and data	1	1

- (1). Notes were purchased by the Bank of North Dakota to fund required reserve funds established by the following series resolutions. The proceeds are invested in certificates of deposit with the Bank of North Dakota. Maturities and interest rates of the bonds and certificates of deposit coincide. The entire amount is noncurrent. (See Note 5).
- (2). The bank investment contract in conjunction with the SRF 2001A bond issue was awarded to the Bank of North Dakota. The investment contract is at a fixed rate and matures on October 1, 2021.

	<u>2005</u>	<u>2004</u>
CFP 1990	\$ 61	\$ 61
CFP 1991	67	67
CFP 1992	15	15
CFP 1993	1,475	1,475
CFP 1994	-	-
CFP 1995	130	458
CFP 1996	361	361
CFP 1997	2,206	2,206
1999 A/B	1,410	1,410
	<u>\$ 5,725</u>	<u>\$ 6,053</u>

NOTES TO FINANCIAL STATEMENTS

NOTE 10 - COMMITMENTS AND CONTINGENCIES

Amounts passed through from the State Department of Health from federal grantor agencies are subject to audit and adjustment by the federal grantor agencies. Any disallowed grant costs may constitute a liability. The amount, if any, of costs which may be disallowed by the grantor will be recognized in the year determined.

The PFA is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Such commitments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet.

The PFA's exposure to credit loss is represented by the contractual amount of these commitments. The PFA follows the same credit policies in making commitments as it does for on-balance-sheet instruments. Commitments to extend credit totaled \$24,160 and \$41,229 as of December 31, 2005 and 2004.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

On April 1, 1997, a Standby Bond Purchase Agreement was executed with the Central Dakota Irrigation District, a political subdivision. Should the District experience financial difficulties, the PFA will purchase Central Dakota Irrigation District's Refunding Improvement Bonds (warrants) in an aggregate principal amount not less than the outstanding principal amount of the warrants plus accrued interest on the warrants. The original principal amount of the warrants issued April 1, 1997 was \$3,270.

The PFA purchased letters of credit from the Bank of North Dakota in order to fund the reserves for the Capital Financing Program Bonds. As of December 31, 2005, \$3,315 of credit was available through these letters of credit and no funds have been advanced.

NOTE 11 - RISK MANAGEMENT

The PFA is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The following are funds/pools established by the State for risk management issues:

The 1995 Legislative Session established the Risk Management Fund (RMF), an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state, its agencies' employees, and the University System. All state agencies participate in the RMF and their fund contribution was determined using a projected cost allocation approach. The statutory liability of the State is limited to a total of \$250 per person and \$1,000 per occurrence.

The PFA also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The PFA pays an annual premium to the Fire and Tornado Fund to cover property damage to personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund. The Fire and Tornado Fund is reinsured by a third party insurance carrier for losses in excess of one million dollars per occurrence during a twelve-month period. The State Bonding Fund currently provides the PFA with blanket fidelity bond coverage in the amount of \$500 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

NOTES TO FINANCIAL STATEMENTS

The PFA, as a contributor to RMF, participates in the North Dakota Workforce Safety and Insurance (WSI), an Enterprise Fund of the State of North Dakota. WSI is a state insurance fund and a "no fault" insurance system covering the State's employers and employees financed by premiums assessed to employers. The premiums are available for the payment of claims to employees injured in the course of employment.

There have been no significant reductions in insurance coverage from the prior year and settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

**NORTH DAKOTA PUBLIC FINANCE
AUTHORITY**

SUPPLEMENTARY INFORMATION

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
COMBINING BALANCE SHEET
DECEMBER 31, 2005
(In Thousands)

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents - unrestricted	\$ -	\$ -	\$ 2,161	\$ 2,161
Restricted				
Restricted cash and cash equivalents	206	75	1,291	1,572
Interest receivable	2,285	1,264	301	3,850
Investments	6,889	911	760	8,560
Municipal securities	5,321	1,918	2,845	10,084
Advance to Bank of North Dakota	-	-	31	31
Total restricted current assets	14,701	4,168	5,228	24,097
Total current assets	14,701	4,168	7,389	26,258
NONCURRENT ASSETS - RESTRICTED				
Investments	88,779	59,360	419	148,558
Municipal securities	98,099	78,321	22,608	199,028
Deferred bond financing costs, net	685	373	204	1,262
Advance to Bank of North Dakota	-	-	5,694	5,694
Total restricted noncurrent assets	187,563	138,054	28,925	354,542
Total assets	\$ 202,264	\$ 142,222	\$ 36,314	\$ 380,800
LIABILITIES				
CURRENT LIABILITIES				
Accounts payable	\$ 1	\$ 1	\$ 14	\$ 16
Rebate due to IRS	215	-	-	215
Bonds payable	4,885	1,735	3,000	9,620
Interest payable	1,052	918	240	2,210
Advance from Bank of North Dakota	-	-	31	31
Total current liabilities	6,153	2,654	3,285	12,092
NONCURRENT LIABILITIES				
Rebate due to IRS	89	189	-	278
Bonds payable, net	76,160	60,923	23,376	160,459
Advance from Bank of North Dakota	-	-	5,633	5,633
Total noncurrent liabilities	76,249	61,112	29,009	166,370
Total liabilities	82,402	63,766	32,294	178,462
NET ASSETS				
Unrestricted	-	-	2,148	2,148
Restricted for debt service	36,231	33,169	1,872	71,272
Restricted for loan purposes	83,631	45,287	-	128,918
Total net assets	119,862	78,456	4,020	202,338
Total liabilities and net assets	\$ 202,264	\$ 142,222	\$ 36,314	\$ 380,800

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
YEAR ENDED DECEMBER 31, 2005
(In Thousands)

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
OPERATING REVENUES				
Investment income	\$ 2,645	\$ 1,692	\$ 1,795	\$ 6,132
Administrative fees and other	517	314	98	929
	<u>3,162</u>	<u>2,006</u>	<u>1,893</u>	<u>7,061</u>
OPERATING EXPENSES				
Interest expense	3,866	2,066	1,922	7,854
State Revolving Fund administration	438	27	-	465
State Revolving Fund set-asides	-	600	-	600
Rebate due to IRS	106	50	-	156
Salaries and benefits	-	-	111	111
Amortization of bond issue costs	125	35	52	212
Operating	-	-	44	44
Paying agent fees	-	-	8	8
	<u>4,535</u>	<u>2,778</u>	<u>2,137</u>	<u>9,450</u>
OPERATING LOSS	<u>(1,373)</u>	<u>(772)</u>	<u>(244)</u>	<u>(2,389)</u>
NONOPERATING REVENUE				
Grant and set-asides	1,068	15,199	-	16,267
Investment income	5,776	2,296	312	8,384
	<u>6,844</u>	<u>17,495</u>	<u>312</u>	<u>24,651</u>
INCOME BEFORE TRANSFERS	5,471	16,723	68	22,262
TRANSFERS	<u>(90)</u>	<u>90</u>	<u>-</u>	<u>-</u>
CHANGE IN NET ASSETS	5,381	16,813	68	22,262
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>114,481</u>	<u>61,643</u>	<u>3,952</u>	<u>180,076</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 119,862</u>	<u>\$ 78,456</u>	<u>\$ 4,020</u>	<u>\$ 202,338</u>

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
COMBINING STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2005
(In Thousands)

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
OPERATING ACTIVITIES				
Receipts of administrative fees from customers	\$ 517	\$ 314	\$ 98	\$ 929
Payments to service providers	(455)	(630)	(49)	(1,134)
Payments to employees	-	-	(112)	(112)
Payment of rebate to IRS	(111)	-	-	(111)
NET CASH FROM (USED FOR) OPERATING ACTIVITIES	(49)	(316)	(63)	(428)
NONCAPITAL FINANCING ACTIVITIES				
Grant and set-asides	1,068	15,199	-	16,267
Transfers	(90)	90	-	-
Interest paid on bonds payable	(3,532)	(1,666)	(1,903)	(7,101)
Bond financing costs	(129)	(157)	-	(286)
Principal payment on advance from Bank of North Dakota	-	-	(388)	(388)
Proceeds from bond premiums	519	697	-	1,216
Proceeds from issuance of bonds payable	11,975	24,235	-	36,210
Principal payments on bonds payable	(11,156)	(3,340)	(4,130)	(18,626)
NET CASH FROM (USED FOR) NONCAPITAL FINANCING ACTIVITIES	(1,345)	35,058	(6,421)	27,292
INVESTING ACTIVITIES				
Interest received on investments and municipal securities	8,294	3,635	2,140	14,069
Collection of advance to Bank of North Dakota	-	-	328	328
Proceeds from maturities and sales of investments	22,346	25,209	1,668	49,223
Purchases of investments	(32,262)	(46,124)	(2,052)	(80,438)
Proceeds from maturities of municipal securities	6,987	3,301	3,940	14,228
Purchases of municipal securities	(4,010)	(20,692)	(7)	(24,709)
NET CASH FROM (USED FOR) INVESTING ACTIVITIES	1,355	(34,671)	6,017	(27,299)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(39)	71	(467)	(435)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	245	4	3,919	4,168
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 206	\$ 75	\$ 3,452	\$ 3,733

(continued on next page)

COMBINING STATEMENT OF CASH FLOWS – Page 2

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
RECONCILIATION OF OPERATING LOSS TO NET CASH USED FOR OPERATING ACTIVITIES				
Operating loss	\$ (1,373)	\$ (772)	\$ (244)	\$ (2,389)
Adjustments to reconcile operating loss to net cash used for operating activities				
Amortization of bond financing costs	125	34	52	211
Net amortization (accretion) of premium (discount) on bonds payable	358	544	45	947
Reclassification of investment income and expense to other activities	863	(169)	80	774
Changes in assets and liabilities				
Accounts payable	(17)	(3)	4	(16)
Rebate due IRS	(5)	50	-	45
NET CASH FROM (USED FOR) OPERATING ACTIVITIES	<u>\$ (49)</u>	<u>\$ (316)</u>	<u>\$ (63)</u>	<u>\$ (428)</u>

NORTH DAKOTA PUBLIC FINANCE AUTHORITY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED DECEMBER 31, 2005

EXHIBIT A-1

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures (In Thousands)</u>
ENVIRONMENTAL PROTECTION AGENCY		
Passed Through the North Dakota Department of Health		
Capitalization Grants for State Revolving Funds	66.458	\$ 1,068
Capitalization Grants for Drinking Water State Revolving Funds	66.468	15,114
State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	66.471	85
Total Environmental Protection Agency		<u>\$ 16,267</u>

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The accompanying schedule of expenditures of federal awards is presented on the accrual basis of accounting.

NOTE 2 - AGENCY OR PASS-THROUGH NUMBER

The pass-through entity has not provided us with the identifying number on all programs, therefore, they are not included in this schedule.

NOTE 3 - SUBRECIPIENTS

Of the federal expenditures presented in the schedule, the North Dakota Public Finance Authority provided federal awards to subrecipients as follows:

<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>(In Thousands)</u>
Capitalization Grants for State Revolving Funds	66.458	\$ 688
Capitalization Grants for Drinking Water State Revolving Funds	66.468	14,755
State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	66.471	85
		<u>\$ 15,528</u>

The above awards consist entirely of loans advanced to the subrecipients.

The North Dakota Public Finance Authority also has outstanding loan balances to subrecipients from prior years. These balances are not included on the accompanying schedule of expenditures and federal awards because the federal government imposes no continuing compliance requirements on the subrecipient.

**NORTH DAKOTA PUBLIC FINANCE AUTHORITY
SUMMARY SCHEDULE OF PRIOR FEDERAL AUDIT FINDINGS
YEAR ENDED DECEMBER 31, 2005**

EXHIBIT A-2

None.



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EXHIBIT A-3, cont.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND OTHER
MATTERS AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

We have audited the basic financial statements of **North Dakota Public Finance Authority**, a component unit of the State of North Dakota, as of and for the year ended December 31, 2005 and have issued our report thereon dated January 25, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered **North Dakota Public Finance Authority's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect **North Dakota Public Finance Authority's** ability to record, process, summarize and report financial data consistent with the assertions of management in the basic financial statements. The reportable condition is described in the accompanying schedule of findings and questioned costs as 2005-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all reportable conditions that also considered to be material weaknesses. However, we believe the reportable condition described above is not a material weakness.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether **North Dakota Public Finance Authority's** basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Bismarck, North Dakota
January 25, 2006



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EXHIBIT A-4

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

Compliance

We have audited the compliance of **North Dakota Public Finance Authority** with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended December 31, 2005. **North Dakota Public Finance Authority's** major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of **North Dakota Public Finance Authority's** management. Our responsibility is to express an opinion on **North Dakota Public Finance Authority's** compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about **North Dakota Public Finance Authority's** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on **North Dakota Public Finance Authority's** compliance with those requirements.

In our opinion, **North Dakota Public Finance Authority** complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2005.

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Internal Control Over Compliance

The management of **North Dakota Public Finance Authority** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered **North Dakota Public Finance Authority's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Bismarck, North Dakota
January 25, 2006

**NORTH DAKOTA PUBLIC FINANCE AUTHORITY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED DECEMBER 31, 2005**

EXHIBIT A-5

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of the North Dakota Public Finance Authority.
2. A reportable condition in internal control was disclosed by the audit of the financial statements. This reportable condition is not considered to be a material weakness.
3. No instances of noncompliance material to the financial statements of the North Dakota Public Finance Authority which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. The auditor's report on compliance for the major federal award program for the North Dakota Public Finance Authority expresses an unqualified opinion on the major federal program.
5. There were no audit findings relative to the major federal award program for the North Dakota Public Finance Authority.
6. The program tested as a major program was #66.468 State Revolving Loan Program – Drinking Water.
7. The threshold for distinguishing a Type A program was \$488,024.
8. The North Dakota Public Finance Authority was determined to be a low-risk auditee.

B. FINDINGS - FINANCIAL STATEMENT AUDIT

2005-1

Statement of Condition

Accounting personnel is responsible for cash receipts, cash disbursements and maintaining the financial reporting system.

Criteria

Segregation of accounting functions necessary to assure adequate internal control.

Recommendation

This is not unusual in organizations of this size, but the Commission should be constantly aware of this condition and realize that the concentration of duties and the responsibilities in a limited number of individuals is not desirable from a control point of view. Under these conditions, the most effective controls lie in the Commission's knowledge of matters relating to the North Dakota Public Finance Authority's operations.

Current Status

Management has addressed the segregation of accounting issue that comes with the small office of the North Dakota Public Finance Authority. Management is working with the Bank of North Dakota to implement additional internal control procedures. With this in mind, procedures have been and will continue to be implemented to provide the highest level of internal control possible.

C. FINDINGS – MAJOR FEDERAL AWARD PROGRAM AUDIT

None.



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EXHIBIT B-1

**NORTH DAKOTA PUBLIC FINANCE AUTHORITY
INDEPENDENT AUDITOR'S SPECIFIC COMMENTS REQUESTED BY THE
NORTH DAKOTA LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE
YEAR ENDED DECEMBER 31, 2005**

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee requires that certain items be addressed by independent certified public accountants performing audits of state agencies. The items and our responses are as follows:

1. Were expenditures made in accordance with legislative appropriations and other state fiscal requirements and restrictions?

Yes.

2. Were revenues accounted for properly?

Yes.

3. Were there adequate financial controls and procedures?

Yes.

4. Was there an adequate and effective system of internal control?

The limited number of office personnel prevents a proper segregation of accounting functions necessary to ensure adequate internal control.

In conjunction therewith, see the reportable condition on internal control in the Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*.

5. Do financial records and reports reconcile with those of state fiscal offices?

Based on our audit procedures, financial records and reports reconciled to data maintained by the Office of Management and Budget.

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6. Was there compliance with statutes, laws, rules and regulations under which the Agency was created and is functioning?

Yes.

7. Was there any indication of fraud or dishonesty?

No.

8. Were there any indications of lack of efficiency in financial operations and management?

No.

9. Was action taken on prior audit findings and recommendations?

Management has addressed the segregation of accounting issue that comes with the small office of the North Dakota Public Finance Authority. Management is working with the Bank of North Dakota to implement additional internal control procedures. With this in mind, procedures have been and will continue to be implemented to provide the highest level of internal control possible.

10. Were all activities of the agency encompassed within appropriations of specific amounts?

All general operating activities are encompassed by appropriations. All other activities are exempt from State appropriations.

11. Has the Agency implemented the statewide accounting and management information system including the cost allocation system?

No. The North Dakota Public Finance Authority has their own accounting system. The uniqueness of the PFA's accounting and management information needs require the PFA to utilize other software systems.

12. Has the Agency developed budgets of actual anticipated expenditures and revenues on at least a quarterly basis and compared on at least a quarterly basis actual expenditures and revenues on the accrual basis to budgeted expenditures and revenues?

No, the PFA has not adopted a formalized budget to actual expenditures due to the fact that not all of their revenue/expenditures fall under a legislative appropriation. However, the PFA does monitor the funds appropriated through the Industrial Commission and our review of the PFA's procedures indicated adequate controls.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.



Bismarck, North Dakota
January 25, 2006